

Benchmark-One™ Series

The Resource - Bottom Line Relationship

"I put 25% on every transaction to cover profit but never seem to get more than 5% at the end of the day. What am I doing wrong?"

The answer lies in the number and profitability of transactions. If the number of transactions is too low, then the desired 25% profit will not be achieved. On the face of it, the number of transactions are too low¹

In order to understand why the transactions are too low, we need to pinpoint the key activity driving them. Some would say marketing is the key activity, but the constraint on output in the non retail sector is invariably man or machine hours. In this case the key driver is man-hours².

Analysis of transactions using the **Tari™ Calculator**, revealed productivity to be 40%.

Assuming prices and quotes have been worked out on the basis of running at say, 70% productivity, then even 5% profit would be a creative achievement in the circumstances.³

The above example highlights the problem likely to arise when management focuses on the profit per without reference to the sum of all transactions for the period to date.

For example, assume a target gross profit⁴ of \$2,000,000 and 20,000 charged hours. The average gross profit per hour would be \$100 and the average weekly gross profit \$4,000 (20,000hrs/50 wks x \$100).

This is where TARI™ comes into play, representing as it does in this case, the \$100 average gross profit per man-hour or 'unit of activity'. It provides a benchmark or index, against which the price of a job can be measured and in turn gives rise to questions: could the job be done in less time and/or could the cost of materials be reduced?

For example, a job priced to sell at \$1300 with \$500 cost of materials and 10 man-hours will return a gross profit of \$80 per unit of activity ($\$1300 - \$500 = \$800 / 10 = \80).

However, if, by reviewing ways and means of improving efficiency, the job took 8 hours, the outcome would be much closer to TARI™: ($\$1300 - \$500 = \$800 / 8 = \100). And if it was possible to cut back the cost of materials to \$300, the result would be better again: [$(\$1300 - \$300) = \$1000 / 8 = \125].

Comparison of actual results with TARI™ x Hours billed for the week and accumulatively for weeks to date, not only ensures the business stays on track, but gives management a clear competitive edge when it comes to winning quotes: **very few businesses know whether their profit is behind or ahead of target when quoting; nor are they aware of the impact a quote may have on the bottom line.**

A business whose results are ahead of target, is in a strong position to knowingly undercut competitors, without denting the bottom line in doing so.

In the next FAQ, we will assess how the use of TARI™ impacts retail/wholesale/ hospitality .

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1 And/or the expenses allocated to the transactions are way under what they should be.

2 In manufacturing/trades/professions the key driver is invariably but not exclusively, man-hours.

3 Expenses/overheads - excluding materials - are allocated to man-hours based on an estimated level of productivity. Obviously if productivity falls below the estimated level, profit will be eroded to the extent that expenses/overheads are under-allocated.

4 Gross profit = [(expenses + profit) - materials at cost]